

INSPECTOR GENERAL'S AUDIT REPORT



U.S. SMALL BUSINESS ADMINISTRATION
OFFICE OF INSPECTOR GENERAL
WASHINGTON, D.C. 20416

AUDIT REPORT

Issue Date: November 15, 2005

Number: 6-04

To: Hector V. Barreto,
Administrator

Tom Dumaresq,
Chief Financial Officer

Robert G. Seabrook

From: Robert G. Seabrooks,
Assistant Inspector General for Auditing

Subject: Audit of SBA's FY 2005 Financial Statements

We contracted with the independent certified public accounting firm of Cotton & Company LLP to audit the financial statements of the U.S. Small Business Administration (SBA) for fiscal years (FY) 2005 and 2004. The contract required that the audit be done in accordance with generally accepted government auditing standards; the Office of Management and Budget's bulletin, *Audit Requirements for Federal Financial Statements*, and the GAO/PCIE *Financial Audit Manual*.

In *The Independent Auditor's Report* the auditor issued an unqualified opinion on the FY 2005 consolidated balance sheet; the related FY 2005 statements of net cost, changes in net position and financing; and the FY 2005 and FY 2004 combined statements of budgetary resources. The auditor issued a qualified opinion on the FY 2004 consolidated balance sheet and the related FY 2004 statements of net costs, changes in net position, and financing. As agreed upon between the Office of the Chief Financial Officer and the Office of the Inspector General, the auditor did not apply all necessary auditing procedures in accordance with generally accepted auditing standards to express an unqualified opinion on SBA's FY 2004 consolidated balance sheet, consolidated statements of net cost, changes in net position, and financing, which the auditor previously issued a qualified opinion on November 15, 2004 (OIG Report No. 05-5). The auditor's opinions on the various financial statements are presented in the chart below.

Auditor's Opinions on SBA's Financial Statements

Statement	FY 2005	FY 2004
Balance Sheet	Unqualified	Qualified
Statement of Net Cost	Unqualified	Qualified
Statement of Changes in Net Position	Unqualified	Qualified
Statement of Budgetary Resources	Unqualified	Unqualified
Statement of Financing	Unqualified	Qualified

The auditor's qualification stemmed from their inability to satisfy themselves as to the reasonableness of SBA's FY 2004 subsidy re-estimates pertaining to its Section 7(a), 504, SBIC Participating Securities, and SBIC Debenture programs, or to the value of Credit Program Receivables and Related Foreclosed Property, Net and Liabilities for Loan Guarantees for these four programs.

The *Independent Auditor's Report on Internal Control* discusses three matters the auditor considers reportable conditions: (1) Financial Management and Reporting Controls; (2) Office of Disaster Assistance Administrative Expenditure Controls; and (3) Agency-Wide Information Systems Controls. The auditors further considered the combined matters described in the first reportable condition to be a material weakness under the standards established by the American Institute of Certified Public Accountants and the OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*, as amended. The auditor also concluded that SBA's control over performance measures did not ensure accuracy and reliability, as required by OMB Circular A-136, *Financial Reporting Requirements* and prevailing accounting literature. The auditor found other management and internal control issues that will be communicated in a separate letter.

In the *Independent Auditor's Report on Compliance with Laws and Regulations* the auditor concluded that SBA was not in substantial compliance with the Federal Financial Management Improvement Act (FFMIA) because of the following: (1) SBA is not in substantial compliance with federal financial system requirements; (2) SBA is not in substantial compliance with federal accounting standards and (3) SBA is not in substantial compliance with the United States Standard General Ledger at the transaction level. Details regarding the matters that led to the auditor's conclusion on SBA's noncompliance with FFMIA are discussed in more detail in the *Independent Auditor's Report on Internal Control*.

The OIG reviewed the auditor's reports and related documentation and made necessary inquiries of its representatives. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on the SBA's financial statements, conclusions about the effectiveness of internal control, conclusions on whether the SBA's financial management systems substantially complied with FFMIA, or conclusions on compliance with laws and regulations. Cotton & Company LLP is responsible for the attached auditor's report dated November 15, 2005, and the conclusions expressed in the report. However, our review disclosed no instances where Cotton & Company LLP did not comply, in all material respects, with generally accepted government auditing standards.

SBA management generally agreed with the auditors' findings and recommendations and noted that they are very pleased that SBA received an unqualified opinion from the independent auditor. Management believes the unqualified opinion is an accurate reflection of the quality of SBA's financial statements and improved accounting, budgeting and reporting processes. Management is disappointed that financial management and reporting controls are still a material weakness and had hoped their hard work over the past several years in this area would have resulted in an improvement to reportable condition. Management understands, however, that additional improvements are required and is committed to maintaining the momentum established this year to improve SBA's financial management processes and results for FY 2006.

The findings in this report are based on the auditor's conclusions and the report recommendations are subject to review, management decision and action by your office, in accordance with existing Agency procedures for follow-up and resolution. Please provide us your proposed management decisions within 30 days on the attached SBA Form 1824, Recommendation Action Sheet.

Should you or your staff have any questions, please contact Jeff Brindle, Director, Information Technology and Financial Management Group at (202) 205-7490.

Attachments